Not cheap or cheerful: south China's new paradigm

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GUANGZHOU, China (AP) — When millions of workers didn't return to their southern China factory jobs after Lunar New Year holidays, a turning point was reached for foreign manufacturers scraping by with slim profit margins.

Companies were already under pressure from rising raw material costs, restive workers and lower payments for exports because of a stronger Chinese currency. Despite hiking wages, labor shortages kept getting worse as workers increasingly spurned the often repetitive and unskilled jobs that helped earn China its reputation as the world's low-cost factory floor.

At one of those factories in an industrial suburb of the southern Chinese city of Guangzhou, a worker uses a sewing machine to stitch together black padding for an orthopedic foot brace. Across the aisle from her, others snip loose threads off disposable cushions for operating tables.

At the end of the shop floor, a young woman glues velcro squares to an elastic strip used to hold an ice bag over an injured leg, churning one out every few seconds using a large machine press.

Later this year, these jobs will be gone as Guangzhou Fortunique's American owner, Charles Hubbs, moves a large chunk of production to Southeast Asia.

"I don't know of any factory in China that can absorb both the raw material prices we have, the labor issues we've been looking at and the renminbi," China's strengthening currency, said Hubbs. The currency is also known as the yuan.

He's joining a wave of export manufacturers, big and small, that are moving from China's coastal manufacturing regions to cheaper inland provinces or out of the country altogether, in a clear sign that southern China's days as a low-cost manufacturing powerhouse are numbered.

Andy Lin, a sales export manager at a small Guangzhou clothing maker, said the owner has opened another factory in Jiangxi province to the north to cope with rising fabric costs and staff shortages. Workers spend grueling 14-hour shifts, with a 90-minute break, sewing casual shirts destined for Japan, Israel, South Korea and Mexico.

Foxconn Technology Group — the world's biggest contract electronics manufacturer with customers including Apple Inc., Sony Corp. and Hewlett-Packard Co. — is planning to gradually cut its workforce of 400,000 in the southern Chinese city of Shenzhen by a quarter and move the bulk of manufacturing inland. Its activities in Shenzhen, which borders Hong Kong, will increasingly turn to research and development with a plan to hire more engineers and designers.

China watchers at Credit Suisse, an investment bank, call the shift an "historical turning point" for China's economy and perhaps the world as the country's role in keeping global inflation low by supplying cheap goods is set to end.

The ripple effects of rising costs in China are already being felt around the globe. U.S. clothing retailers are raising prices for shirts and other garments by 10 percent on average after a decade of price falls, partly due to higher labor costs in China.

"It may take a decade for China to see its export competitiveness erode, but we have seen the beginning of this happening," the Credit Suisse report said, predicting that salaries for China's estimated 150 million migrant workers would rise 20 to 30 percent a year for the next three to five years.

That's partly because China's traditional advantage — its vast, cheap pool of workers — is drying up. Economists say it's the result of a rapidly aging population after 40 years of the one-child policy. Economic growth is "creating more jobs faster than the population is creating new workers," said Stephen Green, an economist at Standard Chartered, in a report titled "Wanted: 25 million workers."

China's blistering growth has also lifted incomes and created more opportunities in poorer inland provinces, which means fewer people leaving for jobs in the richer coastal cities.

Some 30 to 40 percent of migrant workers didn't return to their factory jobs in Guangdong province's Pearl River Delta manufacturing heartland after the annual Lunar New Year holiday in February, said Stanley Lau, deputy chairman of the Hong Kong Federation of Industries. Typically the proportion is 10 to 15 percent.

That was despite Guangdong authorities raising minimum wages by up to 20 percent in March. They're trying to prevent the kind of high-profile labor problems that flared up last year, including a spate of suicides at Foxconn and a series of strikes that disrupted production at factories owned by Honda Motor Co. and Toyota Motor Corp.

Many factories already pay more to retain workers but are still having a hard time finding manpower.

Hubbs employs about 500 workers earning 1,800 to 2,000 yuan ($275 to $306) a month, a lot higher than Guangzhou's 1,300 yuan minimum wage, which came into effect March 1. But he's still short about 100 people, resulting in a 90-day turnaround time for orders, twice as long as he'd like. He wants to move 30 to 40 percent of production to a new factory in Cambodia, Laos or even Myanmar in six to eight months.

He says existing workers won't lose their jobs. Instead they will be moving up the so-called "value chain," transferred to production lines for the company's brand-name line of sterile covers for operating room devices. They require more skilled work but are also more profitable because the company sells them direct to customers instead of through middlemen.

Hubbs has looked at moving elsewhere in China but doesn't think the cost savings would last beyond two or three years as wages and prices even out across the country.

But others such as Dahon, the world's largest maker of folding bicycles, think moving inland will help regain the low cost advantage they once had in southern China.

"It makes sense," chief executive David Hon said. "It could be a year, it could be two, but it seems like we'll be probably moving the bulk of manufacturing elsewhere."

The company is studying sites in central China. It also has been testing out a facility in Tianjin, near Beijing, for two years.

Basic research and development work will remain in Shenzhen, where welders build frames for final assembly at factories in Taiwan, Macau and the Czech Republic.

Greater use of automation is also becoming more economic.

CBL Group, a contract manufacturer, has five welding robots used to assemble brackets for hospital beds and seat frames for new carriages on the New York subway. Chairman Gideon Milstein said he bought them in 2007 and 2008 for $600,000 because they could track welds by computer to ensure they were up to standard.

At the time, it was cheaper to weld by hand but that's changing because wages for skilled human welders are going up.

"It will soon be cheaper to weld by robot than it is by human in China," Milstein said.